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BEFORE THE

DEPARTMENT OF TRANSPORTATION

WASHINGTON, D. C.

Application of AMERICAN AIRLINES, INC. under 49 USC 40109 for exemption (U.S.-Colombia and route integration)	OST-97-2081 – 6
Application of AEROVIAS NACIONALES DE COLOMBIA, S.A. DE C.V. for an exemption from 49 USC 41301	OST-97-2083 – 6
Joint Application of AMERICAN AIRLINES, INC. and AEROVIAS NACIONALES DE COLOMBIA, S.A. DE C.V. for statements of authorization under 14 CFR Parts 207 and 212 (code-sharing)	Undocketed

REPLY OF AMERICAN AIRLINES, INC.

15 pgs

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February 12, 1997

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REPLY OF AMERICAN AIRLINES, INC.

American Airlines, Inc. hereby replies to the answers submitted on February 3, 1997 by Continental Airlines, Inc., Delta Air Lines, Inc., Emery Worldwide Airlines, Inc., and

United Air Lines, Inc. To the extent required, American requests leave to file this reply.'

American and Avianca are seeking authority to engage in reciprocal code-sharing services between the United States and Colombia, within the two countries, and beyond Bogota to certain cities in South America. The proposed code-sharing is consistent with the public interest, as it will expand travel and shipping options available to the public and offer the convenience of on-line services on numerous new routings.

In their answers, the opposing carriers urge the Department to deny the American and Avianca applications because (1) the U.S.-Colombia aviation regime is limited-entry; (2) in their view, American and Avianca "dominate" U.S.-Colombia services; and (3) in their view, American is too strong between the U.S. and Latin America.[2]

'Replies are authorized by 14 CFR 302.407 for the two exemption dockets, but not by 14 CFR Parts 207 or 212 for the undocketed joint application. American's reply should be accepted in the interest of a complete record for the Department's consideration.

[2]In addition, Emery contends that code-sharing authority should be denied because the Government of Colombia has turned down certain of Emery's all-cargo charter requests. Emery ignores the fact that the Miami-Bogota scheduled all-cargo market is one of the most competitive in all of South America, with operations by Aerovias Colombinas (ZU), Challenge Air Cargo (WE), LAC (LC), Millon Air (OX), and Southern Air Transport (SJ) (Cargo OAG, February 1997). Moreover, since the U.S.-Colombia Air Transport Agreement does not provide for all-cargo charters, the Department should reject the suggestion to link such operations to scheduled passenger services in assess-

Such arguments are contrary to well-established Department policy, as well as hypocritical and self-serving. The Department has approved numerous code-sharing arrangements in limited-entry markets. The Department has also approved many such arrangements where the applicants have high combined shares in the country-pair market, as well as where the U.S. carrier partner has a substantial market share in the surrounding region. The proposed arrangement between American and Avianca is consistent with Department policy, will provide significant public benefits, and should be approved without delay.

I. CODE-SHARING APPROVALS IN LIMITED-ENTRY MARKETS

While entry is limited under the U.S.-Colombia Air Transport Agreement, the market is served nonstop by five scheduled combination carriers -- American, Continental, Avianca, ACES, and Aerolineas Argentinas. Continental and ACES account for nearly one-third of the nonstop frequencies operated between the United States and Colombia (OAG, February 1997), and are strong competitors to American and Avianca. Continen-

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ing reciprocity. See, e.g., Order 93-11-22, November 18, 1993, pp. 8-9 (an IATFCPA complaint with respect to passenger services), where the Department refused to include all-cargo services in the proposed sanctions. The Department and Congress have long recognized that all-cargo operations are clearly distinct from combination services, and require special treatment in the development of international aviation policy. See 49 USC 40101(b); Order 89-5-29, May 17, 1989 (Statement of U.S. Inter-national Air Cargo Policy), pp. 5-6.

tal provides the only U.S.-flag nonstop service from the Houston and New York gateways, and is the second largest U.S.-flag carrier to Latin America.

Contrary to the opponents' arguments, open skies or open entry agreements are simply **not** a prerequisite for code-share approvals. Indeed, Continental, Delta, and United have each received approval from the Department for a number of their own code-sharing arrangements with the dominant (or even the monopoly) foreign carrier in numerous limited-entry markets.

- Continental holds authority to code-share with Alitalia (Italy's monopoly flag carrier), notwithstanding the highly restrictive U.S.-Italy Air Transport Agreement. That authorization is extra-bilateral, and the Department recently granted renewal despite the fact that "in the two years since our initial approval, the Italian side has shown no movement in the direction of liberalization, and this despite an accumulation of U.S. carrier aspirations to expand existing services or to introduce new services in the U.S.-Italy market" (Order 96-11-15, November 18, 1996, p. 4). Nonetheless, on February 4, 1997, Continental and Alitalia applied to expand their arrangement even further by adding Atlanta as an additional point (OST-97-2113 and undocketed).

o Delta holds authority to code-share with Varig (Brazil's dominant flag carrier) on an extra-bilateral basis, notwithstanding the limited-entry U.S.-Brazil Air Transport Agreement (Order 94-3-33, March 18, 1994).[3] Delta holds authority to code-share with Aeromexico (which, with its affiliate Mexicana, is Mexico's dominant flag carrier) in the limited-entry U.S.-Mexico market[4] (Order 96-12-8, December 6, 1996, affirmed, Order 97-1-15, January 10, 1997); with Aer Lingus (Ireland's monopoly flag carrier) in the restricted U.S.-Dublin market (Order 96-4-19, April 10, 1996); with TAP-Air Portugal in the U.S.-Portugal market (undocketed, approved under assigned authority, October 11, 1996); and with Virgin Atlantic in the limited-entry U.S.-U.K. market (Order 95-2-28, February 10, 1995). Delta was also granted authority to code-share with Austrian Airlines (Austria's dominant flag carrier) in 1995, at a time when entry restrictions were in force in the U.S.-Austria market (Order 95-2-14, February 7, 1995).

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[3] On February 7, 1997, Delta announced that its code-sharing arrangement with Varig is being terminated.

[4] See Order 96-11-25, November 30, 1996, p. 3 ("[t]he U.S.-Mexico aviation agreement, while more open than in the past, continues to contain restrictions on entry. Specifically, only one carrier from each country may be designated to serve a given city-pair market.... In these circumstances, we must continue to regard the U.S.-Mexico routes as limited-entry").

o United holds authority to code-share with Thai Airways International (Thailand's monopoly flag carrier) in the limited-entry U.S.-Thailand market (Order 96-11-5, November 12, 1996). United holds authority to code-share with Saudia Arabian Airlines (Saudia Arabia's monopoly flag carrier) in the limited-entry U.S.-Saudia Arabia market (Order 96-10-15, October 9, 1996). United is seeking authority to code-share with Mexicana (which, with its affiliate Aeromexico, is Mexico's dominant flag carrier) in the limited-entry U.S.-Mexico market (OST-96-1988 and undocketed). United was also granted authority to code-share with Lufthansa (Germany's dominant flag carrier) in 1993, prior to the U.S.-Germany open skies agreement (Order 93-12-32, December 18, 1993).

In short, there is no principled basis for the Department to reject the American/Avianca proposal because the U.S.-Colombia market has entry restrictions. If that were the Department's standard, the code-sharing authorizations held by Continental, Delta, and United, cited above, should never have been granted, and should now be immediately terminated as contrary to the standard the answering carriers would impose on American.

11. COMBINED MARKET SHARES OF CODE-SHARING PARTNERS

The opponents further contend that the American and Avianca applications should be denied because of the combined share of the two carriers in the U.S.-Colombia market. That has not been the standard in other code-sharing decisions, and there is no compelling reason for the Department to adopt such a standard here.

The combined market share of American and Avianca between the United States and Colombia is far lower than the combined shares held by U.S. carriers and their foreign-flag partners in a number of other code-sharing proceedings where the Department granted authority. For example, in the Delta/ Aer Lingus code-share, the two carriers operate 100 percent of the nonstop seats between the United States and Dublin (OAG, February 1997). In the United/Saudia Arabian Airlines code-share, the two carriers operate 100 percent of the nonstop seats between the United States and Saudia Arabia (id.). Moreover, in both of these examples, not only are there restrictions under the applicable bilateral agreements, but unlike the situation in Colombia, the foreign code-share partner is the monopoly flag carrier in the respective country.

The opposing carriers have not cited any Department decisions that have used the combined market share of code-sharing partners as the standard. And, as shown above, the

Department has granted code-sharing applications where combined market shares are 100 percent. There is no principled basis for the Department to deny the American/Avianca proposal because of the applicants' combined share of the U.S.-Colombia market.

III. THE U.S. PARTNER'S "REGIONAL" STRENGTH

Finally, the opposing carriers contend that American's regional strength in Latin America should preclude authorization for code-sharing with Avianca. Again, the Department has not used any such standard in its decisions.

To the contrary, United made a similar argument when it opposed American's request for additional frequencies to serve the U.S.-Argentina market. In that proceeding, United argued that its application for additional frequencies should be granted -- and American's application should be denied -- "because of the competitive situation in Latin America as a whole" (Order 94-9-36, September 26, 1994, p. 4). The Department explicitly rejected such a theory, stating that "we do not believe that [American's] proposal in this case, which would produce a limited incremental competitive change in a single Miami-South American market, would provide a significant impact on the competitive structure in Latin America" (id., affirmed, Order 95-2-23, February 18, 1995). The Department should reach a similar conclusion here.

Moreover, United hardly has standing to postulate that an applicant's regional strength is a valid reason to deny code-sharing authority. United is without question a dominant carrier in the Pacific, and yet holds authority to code-share with Thai International Airways, as noted above, and is seeking authority to do so with Air New Zealand (OST-96-1143 and undocketed). If the Department were to apply United's theory to United, neither of those code-shares would be permitted. Again, opponents are urging a decisional standard that they would not have the Department apply to their own arrangements.[5]

[5] In addition, United generally complains about American's strength at the Miami gateway. In approving the American-Eastern route transfer in 1990, the Department anticipated that American would be a strong and vibrant competitor, and would improve service to the public. American has done so. United, on the other hand, has been a lackluster competitor in Latin America. United has failed to devote resources to build a hub at Miami to take advantage of connecting flows. United has failed to enter numerous open-entry markets throughout the region to compete with American, other U.S.-flag carriers, and foreign carriers. United has even failed to use all of its frequencies in limited-entry markets, including Brazil and Argentina. Moreover, in light of its own actions in the Pacific, United has no standing to criticize American's expansion in Latin America. In the Pacific Division Transfer Case in 1985, United said it would double Pan Am's capacity, and it did so during a period when other carriers serving Japan has virtually no opportunity to respond.

IV. PUBLIC BENEFITS OF THE AMERICAN/AVIANCA CODE-SHARE

The proposed code-sharing arrangement between American and Avianca will provide substantial public benefits, and should be approved without delay.

In the U.S.-Colombia market, nonstop service is provided in 12 city-pairs.[6] American and Avianca have overlapping operations in only two -- Barranquilla-Miami and Bogota-Miami (where ACES also provides nonstop service).

This code-share will give American its first access to Medellin, as well as to numerous other points within Colombia where there is currently no U.S. flag service. The arrangement will allow Avianca the opportunity to strengthen itself and become a more effective competitor in preparation for liberalization of the U.S.-Colombia aviation relationship, and will facilitate the resumption of Category I status.

The proposal will also afford broad opportunities for improvements in passenger service, and pro-competitive efficiencies that will lower costs and benefit passengers. On overlapping routes, the relationship between American and Avianca will continue to be competitive. Competitive pressures

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[6] Barranquilla-Miami (AA, AV), Barranquilla-New York (AV), Bogota-Houston (CO), Bogota-Los Angeles (AR), Bogota-Miami (AA, AV, VX), Bogota-New York (AV, CO), Bogota-San Juan (VX), Cali-Miami (AA), Cartegena-Miami (AV), Cartegena-New York (AV), Medellin-Miami (VX), Medellin-New York (AV) (OAG, February 1997).

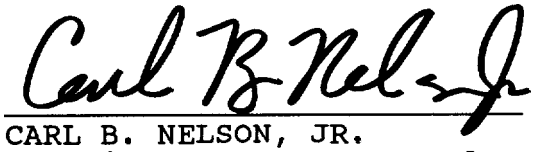
will force the airlines to match one another's prices, and customer service will become an important competitive factor. Under these circumstances, customers will benefit as each airline ensures that it delivers the best service.

Each carrier will benefit from expanded marketing of its services by the code-share partner. To the extent that each carrier attracts incremental traffic as a consequence of its partner's marketing, that will increase efficient utilization of aircraft, and result in lower unit costs. The structure of the code-share arrangement between American and Avianca leaves incentives for vigorous price competition between the parties fully intact. As operating costs are decreased through efficiency gains, competition between the parties and with other airlines will tend to drive fares down, as each airline strives for a greater share of the total market and seeks to stimulate additional traffic. The net result will be a more competitive marketplace, consistent with the Department's policy favoring code-sharing in the international arena.

CONCLUSION

The proposed American/Avianca arrangement will provide distinct pro-competitive benefits, including the strengthening of Avianca in preparation for a liberalized U.S.-Colombia aviation agreement. The answering carriers have provided no principled rationale for their opposition, particularly in light of their own code-shares with other foreign carriers in other limited-entry international markets. The captioned applications should be promptly approved.

Respectfully submitted,



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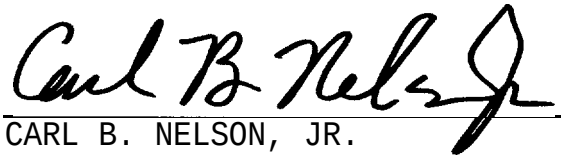
Associate General Counsel
American Airlines, Inc.

February 12, 1997

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing reply by first-class mail on all persons named on the service list attached to the joint application, and on Delta Air Lines, Inc. and Emery Worldwide Airlines, Inc.



CARL B. NELSON, JR.

February 12, 1997